

FDIC State Profile

Winter 2005

Puerto Rico and the U.S. Virgin Islands

Employment growth in Puerto Rico has declined, while job growth in the U.S. Virgin Islands (USVI) has improved.

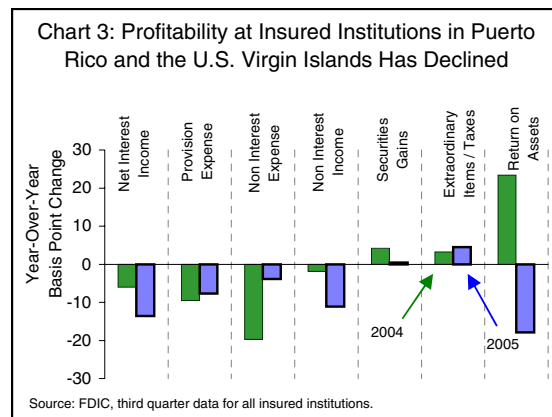
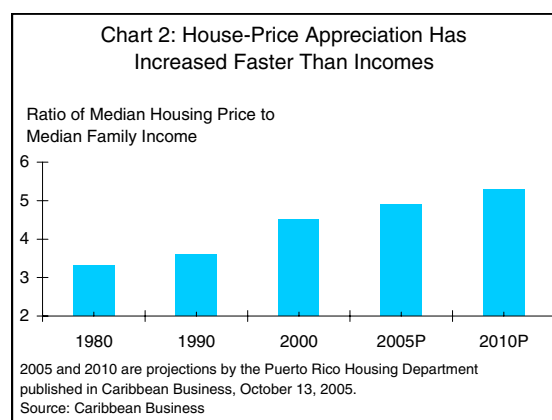
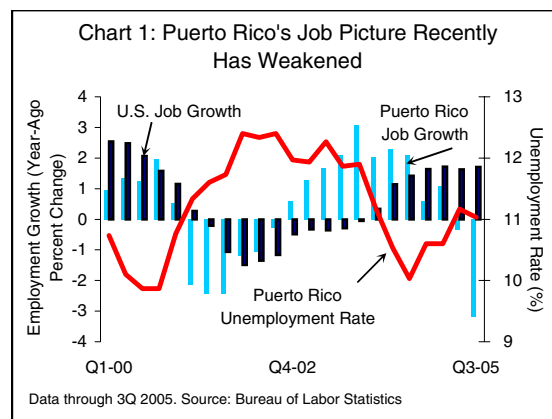
- Puerto Rico's job picture softened in third quarter 2005, with the first back-to-back negative quarterly job growth since 2002 (see Chart 1). Reflecting the job weakness, Puerto Rico's unemployment rate rose over the past year but remained significantly below recession levels.
- Competition for manufacturing jobs from other countries has contributed to continued manufacturing job declines in Puerto Rico. In addition, for the first time in several years, Puerto Rico experienced job losses in the education, health, and government sectors.
- Employment growth in the USVI improved in third quarter 2005 based on a rebound in retailing and construction. However, employment related to tourism, the USVI's most important industry, was negative for the past three quarters. The frequent and large number of hurricanes in 2005 may have contributed to reduced travel to the area.

Tourism continues to be an important component of Puerto Rico's economy.

- Puerto Rico's hotel occupancy rate declined two points to 80.7 percent for the year ending July 2005 compared with the prior year's period. Despite the slight decline, hotel occupancy among Puerto Rican hotels was significantly higher than the U.S. average and compared favorably with top tourist destinations such as Honolulu and New York City in 2005.¹
- Puerto Rico's convention traffic may increase over the short-term because of damage to convention sites in New Orleans from Hurricane Katrina.

Puerto Rico is very oil dependent.

- Because Puerto Rico is heavily reliant on oil for its energy needs, rising crude oil prices in 2005 could have a major impact on consumption. Puerto Rican consumers used 1.2 billion gallons of gasoline in 2004, spending \$217



¹Government Development Bank of Puerto Rico and Property and Portfolio Research.

million. Puerto Rico relies on oil for about 70 percent of its energy needs, more than any state in the U.S.

Personal bankruptcy filings have increased but remained below previous highs.

- A combination of factors, including high energy costs and rising interest rates, may stress some of the Puerto Rico's consumers this winter. Per-capita personal bankruptcies increased nationally and in Puerto Rico prior to the enactment of the new U.S. bankruptcy law in October 2005.² While increasing during most of 2005, per capita personal bankruptcy filings in Puerto Rico remained lower than the area's previous high reached in mid-1998.
- Puerto Rico's 13 percent increase in the per capita personal bankruptcy rate (year over year) during the third quarter 2005 was the area's largest quarterly increase in two years but significantly lower than the U.S. increase of 36 percent.

Housing affordability has declined in Puerto Rico.

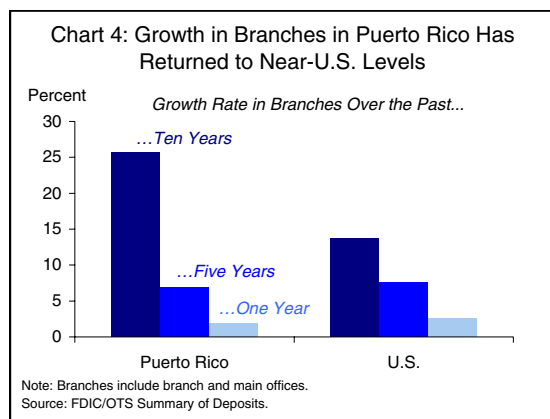
- Local reports suggest that home price appreciation in Puerto Rico has significantly outpaced family income growth, making it more difficult for the average family to purchase a single-family home.
- Estimates suggest that Puerto Rico's ratio of home prices to income was 4.5 times at the beginning of the decade (see Chart 2).³ This figure was double the U.S. average. Projections by the Puerto Rico Housing Department suggest that the ratio of home appreciation to income will continue to increase.

The flatter yield curve has pressured bank profitability.

- The profitability (return on assets) for institutions headquartered in Puerto Rico and the USVI declined in third quarter 2005 compared with the similar 2004 period.
- Securities gains and lower operating and provision expenses only partially offset the effects of decreased net interest income and non-interest income (see Chart 3).
- The flatter yield curve has constrained net interest margins, which have declined for five consecutive quarters. The yield curve has flattened by approximately 200 basis points between third quarters 2004 and 2005.⁴
- Despite lower profitability, credit quality trends were favorable as the ratio of past-due to total loans improved from the similar 2004 period.

Branch growth has slowed and approximated the U.S. growth rate during the past year.

- Annual Summary of Deposit data collected by the FDIC shows growth in bank branches in Puerto Rico has returned to a rate comparable to the United States (see Chart 4). Puerto Rico ranked 13th highest in branch growth with U.S. states over the past ten years, but ranked 30th in the past year.⁵
- As branch growth has slowed, deposits-per-branch has increased from \$58 million per branch to \$96 million over the past five years. Nevertheless, deposit gathering remained very competitive in Puerto Rico, partly because of its large unbanked population.
- Some local institutions have expanded outside Puerto Rico to grow core deposits. Additionally, some large mainland U.S. banks have exited the market during the past decade. The number of out-of-area banks with branches in Puerto Rico has declined from 24 to 17 since 1994.



²Sources: Administrative Office of the U.S. Courts/Haver Analytics, Moody's Economy.com, FDIC.

³Carlos Marquez and Angel C. Tavaréz, "The Challenges of Building in Puerto Rico," *Caribbean Business*, October 13, 2005, pp. 16-20.

⁴The yield curve is measured by the difference between the yield on ten-year and three-month U.S. Treasury securities.

⁵Data as of June 30, 2005. <http://www2.fdic.gov/sod>. Bank branches include branches and main offices.

Puerto Rico and the U.S. Virgin Islands at a Glance

ECONOMIC INDICATORS (Change from year ago, unless noted)

Employment Growth Rates	Q3-05	Q2-05	Q3-04	2004	Q3-04
Total Nonfarm (share of trailing four quarter employment in parentheses)	-3.2%	-0.3%	2.1%	1.7%	2.0%
Manufacturing (11%)	-1.6%	-1.0%	0.3%	-0.3%	-2.4%
Other (non-manufacturing) Goods-Producing (6%)	-4.9%	-2.4%	-0.8%	-0.9%	-2.3%
Private Service-Producing (53%)	-1.4%	-0.4%	2.6%	2.2%	3.8%
Government (29%)	-6.6%	0.4%	2.5%	2.4%	1.8%
Unemployment Rate (% of labor force)	11.0	11.2	10.0	10.6	12.0

BANKING TRENDS

General Information	Q3-05	Q2-05	Q3-04	2004	Q3-04
Institutions (#)	12	12	12	12	13
Total Assets (in millions)	101,651	100,965	90,430	93,703	78,275
New Institutions (# < 3 years)	0	0	0	0	0
Subchapter S Institutions	1	1	1	1	1

Asset Quality	Q3-05	Q2-05	Q3-04	2004	Q3-04
Past-Due and Nonaccrual Loans / Total Loans (median %)	3.59	3.66	4.31	4.35	4.80
ALLL/Total Loans (median %)	1.12	1.14	1.33	1.28	1.55
ALLL/Noncurrent Loans (median multiple)	0.55	0.57	0.59	0.55	0.62
Net Loan Losses / Total Loans (median %)	0.27	0.44	0.29	0.51	0.37

Capital / Earnings	Q3-05	Q2-05	Q3-04	2004	Q3-04
Tier 1 Leverage (median %)	6.72	6.93	6.91	6.88	6.78
Return on Assets (median %)	0.92	1.00	1.33	1.35	1.16
Pretax Return on Assets (median %)	1.15	1.36	1.68	1.65	1.37
Net Interest Margin (median %)	2.84	3.15	3.24	3.21	2.96
Yield on Earning Assets (median %)	5.72	5.68	5.17	4.98	5.35
Cost of Funding Earning Assets (median %)	2.90	2.57	2.02	2.00	2.36
Provisions to Avg. Assets (median %)	0.21	0.18	0.33	0.31	0.42
Noninterest Income to Avg. Assets (median %)	0.41	0.46	0.58	0.62	0.64
Overhead to Avg. Assets (median %)	1.66	2.01	2.01	2.13	2.23

Liquidity / Sensitivity	Q3-05	Q2-05	Q3-04	2004	Q3-04
Loans to Assets (median %)	55.2	53.9	55.0	54.4	55.0
Noncore Funding to Assets (median %)	65.5	63.2	57.5	59.1	59.7
Long-term Assets to Assets (median %, call filers)	42.2	44.1	41.5	40.1	39.9
Brokered Deposits (number of institutions)	9	9	9	9	10
Brokered Deposits to Assets (median % for those above)	14.8	12.4	11.1	11.3	13.7

Loan Concentrations (median % of Tier 1 Capital)	Q3-05	Q2-05	Q3-04	2004	Q3-04
Commercial and Industrial	123.2	105.6	96.2	83.9	143.3
Commercial Real Estate	201.8	184.9	184.4	175.6	194.0
Construction & Development	57.8	51.7	41.7	39.8	58.5
Multifamily Residential Real Estate	0.0	0.2	0.2	0.2	0.0
Nonresidential Real Estate	119.0	119.2	124.5	120.8	143.7
Residential Real Estate	242.5	243.5	287.4	251.7	306.0
Consumer	38.1	40.4	53.1	49.1	90.0
Agriculture	3.2	3.9	3.2	3.1	0.1

BANKING PROFILE

Largest Deposit Markets	Institutions in Market	Deposits (\$ millions)	Asset Distribution	Institutions
San Juan-Caguas-Guaynabo, PR	11	47,416	< \$250 million	2 (16.7%)
Ponce, PR	11	1,849	\$250 million to \$1 billion	0 (0%)
Mayaguez, PR	11	1,239	\$1 billion to \$10 billion	6 (50%)
Aguadilla-Isabela-San Sebastian, PR	8	1,181	> \$10 billion	4 (33.3%)
San German-Cabo Rojo, PR	4	702		